UNITED STATES OF AMERICA
BEFORE THE
FEDERAL TRADE COMMISSION

Comments Regarding Retail Electric Competition	))	V010003

COMMENTS OF THE ELECTRIC POWER SUPPLY ASSOCIATION

I. Introduction

The Electric Power Supply Association (EPSA) is pleased to submit the following comments in response to the Federal Trade Commission's (Commission) Notice Requesting Comments on Retail Electricity Competition Plans. The Commission has recognized a number of significant issues facing the electricity industry in its attempt to examine the many regulatory and legislative approaches states have taken to restructure their electricity markets.

EPSA is the national trade association representing competitive power suppliers, including independent power producers, merchant generators and power marketers. EPSA members provide reliable, competitively priced electricity from environmentally responsible facilities in U.S. and global power markets. EPSA seeks to bring the benefits of competition to all power customers.[1]

[1] The comments contained in this filing represent the position of EPSA as an organization, but not necessarily the view of any particular member with respect to any issue.

EPSA believes that all consumers should have a choice of electricity suppliers. To date, 25 states and the District of Columbia have taken steps to restructure their electricity industry to give customers that choice. Competition is the most effective tool to enhance reliability, bolster economic development, provide new services to consumers and keep prices as affordable and stable as possible. While acknowledging that every state is unique, EPSA believes that every consumer nationwide can and will benefit from having a choice of electricity suppliers.

In November 2000, EPSA published a revised version of its white paper, *Retail Competition: Getting It Right!* This document includes detailed recommendations regarding the issues encountered by states that have already implemented retail electricity competition. Among its conclusions, EPSA recommends that states ensure a "date certain" when competition will begin; create effective customer choice through the unbundling of utility services; guarantee the full recovery of all legitimate, verifiable, non-mitigable, prudently incurred, net (eligible) stranded costs; provide open and fair access to the transmission and distribution system for all suppliers; establish regional transmission organizations (RTOs); and eliminate barriers to participation in a competitive market. A copy of the white paper is attached for the Commission's consideration. Further, EPSA would like to expand on a few critical issues that are affecting retail markets in states that have already opened to competition.

For ease of reading, EPSA's comments track the identification of issues in the Commission's notice. Given that EPSA represents competitive power suppliers

nationwide, we will not respond to every question in the Commission's notice, but will instead discuss the issues on a broader basis. EPSA member companies will submit their experiences in state retail markets in greater detail in their filings with the Commission.

II.
Switching Requirements

There are several aspects of switching rules that are critical to the successful development of retail markets. Uniform business rules for switching customer accounts are necessary for a properly functioning competitive marketplace. High exit fees are a significant barrier to competitive suppliers in developing markets, since high customer acquisition costs discourage participation in retail markets. Lengthy notice periods before consumers can switch to a new electricity supplier also pose a threat to market entrants. Another important issue associated with customer switching policy is whether a customer must provide signed authorization before their distribution company may switch them to another supplier. A signed authorization has often been viewed as the best method to prevent "slamming." However, signature requirements provide a significant advantage to existing utilities, as the signature acts as a barrier to contracts with competitive suppliers. If a customer initiates contact with its distribution company to authorize the switch and provides identifying information, additional barriers to finalize this transaction should not be imposed. The distribution company's only obligation should be to record the change for billing purposes. Customers who are solicited by a supplier to switch should not be switched until the new supplier obtains authorization in

one of three methods: oral verification by an independent third-party, electronic verification or written authorization.

III.
Provider of Last Resort

The importance of provider of last resort (POLR) issues to the development of competitive markets cannot be overstated. In the transition to a fully competitive market, legislators, regulators and consumer advocates have been understandably concerned about ensuring small customers receive continued generation service at a reasonable price. Customers should be assured a continuous source of electricity, even if they do not choose a new supplier. In addition to those customers who choose not to choose, other customers who must also be assured access to electricity include: (1) customers who need POLR service because they are unable or unqualified to obtain service from a competitive power supplier, and (2) customers whose service has, for whatever reason, been terminated by their supplier and who need "backstop" service. State regulators must decide who will provide the electricity service to these customers. It is important that policymakers design POLR programs to maximize customers choice, and minimize the number of customers who take POLR service.

Allowing new market entrants (including competitive utility affiliates) to bid to provide POLR service is essential. If customers can, by not choosing, remain with the incumbent utility, then the incumbent utility has gained a significant competitive advantage. Competitive suppliers will have a tremendous struggle to break in to the market, which may discourage them from doing so.

IV.
Artificial Price Caps

The price customers see for retail electricity service needs to account for changing market conditions, as well as the full costs of providing the service. For competition to work, consumers must see real market prices and the pricing of electricity service should be responsive to changes in wholesale market prices. Knowing the real economic cost of electricity will enable consumers to make informed decisions about when and how to use electricity efficiently. Regulators should not allow administratively fixed or artificially capped or controlled rates in a competitive market, as it will only stunt the development of such a market. Controlled prices do not protect consumers, turning high prices into shortages instead. In addition, price controls do harm in four areas. They (1) stifle competitor entry into the market, (2) stifle the introduction of risk-mitigation products, (3) prevent demand-side response to supply shortages, and (4) divert attention from the need for structural change.

Price controls stifle entry by inhibiting market prices from rising to a level necessary to justify investment. It is not appropriate for policymakers to guess at what that price is and to set a cap based on that guess. Market conditions vary too much to expect that guess to be right. A well-structured market is self-correcting. If prices rise above the level necessary to justify entry, then market entrants responding to these price signals will bring those prices down. Accurate price signals are needed to encourage suppliers to make capacity and energy available to provide ancillary services and replacement reserves or, if necessary, to finance and develop new generation

projects. Manipulating the market price by imposing price controls will distort market price signals and chill development of new generation because of uncertain market prices. Price-controlled markets are inherently viewed as both riskier and less profitable to competitive power suppliers. Price controls and trading limits increase risk, because there is no guarantee that, once set, such caps or limits would not be tightened in the future. Moreover, price caps and trading limits would deny suppliers of electricity the opportunity to cover their fixed costs during those important, but transitory, periods when market prices substantially exceed long-run average costs. Nor is this increased risk offset by symmetric assurances of price floors. In short, the best defense against price spikes is to encourage greater numbers of suppliers to enter the market, not to restrict the payments to existing suppliers.

Price controls can also stifle the introduction of risk-mitigation products. Without an incentive to manage demand or hedge risk, load-serving entities (LSEs) create a "vertical price curve," in which the value of the "last megawatt" is infinite. In this scenario, price caps become the only logical solution. This approach, however, is self-perpetuating and fails to lead to a more lasting solution. Price controls eliminate incentives for LSEs to hedge risk, either physically or financially. In fact, LSEs are given a free regulatory hedge to the disadvantage of other competitive market participants who invest in hedging "tools" and learn to manage risk appropriately. With perpetual "training wheels," LSEs never learn to manage the risks inherent in a competitive market. Problems are postponed, but not solved.

Price controls also prevent demand-side response to rising prices. For competitive markets to flourish, supply and demand must interact freely to determine the price, thereby allowing market participants to make intelligent resource allocation decisions. At just the time when we need to attract capital for new generation and to expand and improve the electric system infrastructure, price controls will create uncertainty that will discourage and delay this much-needed investment. This narrow speculation regarding demand-side responsiveness amounts to a high stakes gamble that consumers will be harmed more by short-lived, infrequent price spikes than by long-term delays in generation investment needed for reliability. Rather than speculative short-term outcomes, the wiser approach to both price spikes and reliability concerns is to unleash free market forces and the investment capital they will provide.

Finally, price controls divert policymakers from making the structural changes necessary to assure a fully competitive market that offers competitive prices, low risk, high reliability and superior environmental performance. Policymakers should concentrate on developing market-oriented solutions to any remaining market flaws, rather than engaging in heavy handed intervention by capping competitively-determined prices

V.
Aggregation

There is every indication that residential customers can benefit significantly from competition. Residential customers can benefit directly from all the cost efficiencies and service gains competition will deliver. The aggregation of residential and small business

customer needs could well result in additional savings. Aggregation provides opportunities for small customers who may not otherwise be the target of marketing efforts by energy suppliers to participate in and benefit from the competitive market. Through aggregation, small customers are able to pool their purchasing power and wield the same influence as large customers. As the competitive market evolves, aggregators may also be able to secure valuable services, such as consolidated billing, energy management services, and energy use analysis for small customers. Moreover, some suppliers will offer other services with electric supply, such as natural gas supply, long-distance telephone service, Internet access and cable service. Aggregation is an increasingly effective tool for maximizing savings and mitigating risk in the competitive power market. For instance, Green Mountain Energy was selected in February to serve more than 400,000 electricity customers in Ohio in the nation's largest-ever energy aggregation contract to date. The Northeast Ohio Public Energy Council formed the electricity buying group to serve nearly 100 communities in the state.

VI.
Market Structure

Wholesale and retail markets are two sides of the same coin. A healthy wholesale market is a critical element of a well-functioning retail market. If wholesale markets don't work, retail suppliers cannot provide customers with products that meet their needs. On the other hand, poorly functioning retail markets mask price signals, thereby depriving consumers and retail suppliers of the ability to use appropriate demand-side and hedging tools to manage wholesale price volatility. In a properly-functioning competitive electricity market, wholesale competition will manage the

supply, and retail competition will manage the demand. It is the job of LSEs to effectively manage risk through bilateral agreements and other financial tools. Continual retail rate freezes discourage large and small customers from implementing load management programs or securing risk-management products from other energy service providers.

VII.
Generation Supply

Competition in the wholesale electric generation business is quickly becoming the principle way additional demand for electricity is being managed across the county. Merchant power plants have become the dominant source of new power generation throughout the U.S. Merchant plants are designed to compete in the wholesale and retail markets, as well as to help maintain and enhance the reliability of regional electricity systems.

Regulators and legislators must develop rules that (1) relieve merchant power plant developers of the requirement to obtain a certificate of need and necessity; (2) encourage consistent, fair, non-discriminatory and workable interconnection policies; and, (3) control and mitigate market power problems. Adopting rules and policies that promote the development of merchant power plants provides numerous benefits, ranging from lower costs, environmental improvements, as newer facilities replace older generation assets, minimizing incumbent utilities' vertical and horizontal market power, to providing the liquidity needed to support robust wholesale trading. Further, market signals are much faster than regulatory processes, so market incentives are a more

efficient means of ensuring that sufficient capacity exists to meet demand on the system.

Generating facilities that competitive power suppliers construct are built at stockholder risk. This shifting of risk from utility ratepayers to merchant power investors indicates that, with respect to development projects financed by new entrants, certificates of need are obsolete. Experience with the emerging markets has demonstrated that the competitive pressures of supply and demand are an effective substitute for a regulatory certification process, particularly where private stockholders, not ratepayers, are at risk. In light of the availability and willingness of competitive power suppliers to meet the nation's electricity needs, there is no reason to require utility ratepayers to bear the risks associated with utility investment in power generation when other market participants can insulate consumers from those risks.

VIII.
Interconnection

To obtain the benefits from competitive generation, merchant power plant developers must be able to reach consumers. Thus, it is also essential to promote policies that provide for consistent, fair and workable interconnection rules and procedures. EPSA ultimately hopes that the Federal Energy Regulatory Commission will order standard interconnection procedures. However, EPSA encourages state regulatory commissions to require jurisdictional utilities to develop clear and consistent interconnection policies, with definitive timelines for action, confidentiality guidelines and

standardized interconnection agreements to meet their regional needs. Clear and efficient interconnection procedures are critical to developing, maintain and enhancing competitive electric power markets. Uniform business practices would allow generation developers, many of whom are national companies, to develop more streamlined procedures for their project developments. There is no reason for these requirements to vary from transmission provider to transmission provider.

IX.
Comparable Transmission Service

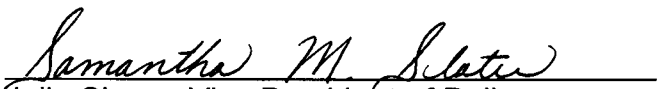
The development of a seamless national transmission system wherein all transmission usage is accorded fully comparable treatment is vitally important to the growth of a competitive power industry. EPSA believes that the establishment of RTOs represents one of the next step towards that end. The prospect of real competition continues to be threatened by, among other things, the manifest lack of comparability between certain wholesale and retail transmission pricing and access policies resulting from the discriminatory exemption of all native load from open access rules. The elimination of residual discrimination will occur only when all uses of the transmission grid are under the same rate schedules, terms and conditions. With actual comparability, the transmission owner's interest would be to operate the grid as a stand-alone business and maximize throughput, rather than to use transmission to increase the return on its investment in power generation, marketing and sales. With its incentives aligned in this manner, the transmission operator could be expected to pursue those regional combinations that make the most business sense. Thus, comparability is critical if competitive power markets are to achieve their full potential.

X.
Conclusion

EPSA commends the Commission for its initiative and thanks the Commission for this opportunity to express its views on some of the issues that have been presented. EPSA hopes that its Comments will assist the Commission in its determinations about how to proceed on these important issues. If you have any additional questions regarding these issues, please don't hesitate to contact us. We are happy to be an ongoing information resource for you and your staff, and to serve as a liaison with our membership.

Dated: April 3, 2001

Respectfully submitted,



Julie Simon, Vice President of Policy
Samantha M. Slater, Manager of State & Regional Affairs
ELECTRIC POWER SUPPLY ASSOCIATION
1401 New York Avenue, N.W.
11th Floor
Washington, D.C. 20005
Telephone: 202-628-8200
Fax: 202-628-8260
E-mail: sslater@epsa.org